PERS-06 MODIFY THE FEDERAL EMPLOYEES HEALTH BENEFITS PROGRAM

Savings from CBO Baseline	Annual Outlay Savings (millions of dollars) 1987	1988	1989	1990	1991	Cumulative Five-Year Savings
Budget Authority	60	120	190	270	360	1,000
Outlays	60	120	190	270	360	1,000

The Federal Employees Health Benefits (FEHB) program offers health insurance coverage for federal employees and annuitants (that is, retirees) and their dependents. In 1985, the program covered about 3.8 million enrollees at an annual premium cost to the federal government of approximately $3.3 billion. About half of this amount was paid to hospitals for services provided to FEHB enrollees.

Program costs could be reduced by reforming hospital reimbursement procedures. Currently, FEHB insurance carriers pay hospitals on a "reasonable" cost basis. An alternative reimbursement system could require carriers to use a prospective payment system similar to that now used by Medicare. Under Medicare, hospitals receive a flat payment per case based on a patient's diagnosis. Applying a similar reimbursement system to FEHB based on diagnosis-related groups (DRGs) would entail modifying the payment schedule to reflect the health care needs of younger patients. Any hospital that accepts federal reimbursement from Medicare could be required to accept the predetermined rate as payment for FEHB enrollees. A hospital would be prohibited from charging enrollees more than the DRG amount the carriers are required to pay.

Savings realized by FEHB insurance carriers under this prospective payment system would allow for lower premium payments by both enrollees and the federal government. The five-year savings of $1 billion shown above represents only the federal budgetary savings. This estimate assumes that annual increases in DRG reimbursements would be tied to the hospital price index plus an additional 0.25 percent to permit technological advances. (The President's budget proposes a voucher system that would limit the annual rise in agency FEHB premiums to the implicit price deflator for the gross national

product. If implemented on schedule, it would reduce outlays through 1991 by nearly $5 billion.)

Advocates of bringing FEHB under a prospective payment system argue that hospitals would be less able to shift costs from Medicare to other third-party payers, like FEHB carriers, that currently reimburse without DRG limits. In addition, some proponents believe that an expanded DRG reimbursement system would also reinforce existing incentives for hospitals to contain costs. In their view, the current system drives up costs because hospitals tend to provide FEHB patients more amenities, more technology, and more staff than are necessary. A DRG system, by contrast, seeks to increase hospital efficiency while maintaining the quality of health care.

Opponents of this proposal would voice many of the same concerns about jeopardizing quality health care that were raised during debate on adopting the DRG scheme for Medicare. Because the payment does not recognize costs actually incurred on behalf of each patient, hospitals would profit from cases where a patient was healthier than average, and would suffer a financial loss when a patient was sicker than average. Under such economic incentives, opponents argue, hospitals might avoid treating patients with severe illnesses, might encourage profitable admissions of those with minor health problems who do not necessarily require hospitalization, and might discharge some patients prematurely. Some critics are also concerned that over time DRG relative prices might diverge from costs, causing hospitals to accentuate the selection of patients on the basis of profit considerations. In addition, hospitals might incur excessive costs to set up a DRG accounting system to serve the relatively small numbers of younger FEHB patients in many areas.

PERS-07 REDUCE FEDERAL TRAVEL EXPENSES

Savings from CBO Baseline	Annual Outlay Savings (millions of dollars) 1987	1988	1989	1990	1991	Cumulative Five-Year Savings
Budget Authority	580	610	650	690	730	3,260
Outlays	530	560	600	630	670	2,990

The Executive Branch spends about $6 billion a year on employee travel. Appropriation action requiring a 10 percent across-the-board cut in travel expenses would save, relative to the CBO baseline, about $3 billion over five years. About 70 percent of this savings would arise from reductions in military travel. Although travel estimates vary widely among individual accounts, the totals in the President's budget reflect a slight decrease relative to the 1987 baseline estimates, with amounts for military travel growing at a faster rate than those for civilian employee travel.

The General Services Administration (GSA) and Department of Defense (DoD), which manage travel arrangements for civilian and military personnel, respectively, report that recent improvements in procurement methods have reduced government travel expenses. Despite these achievements and an across-the-board limit on the 1982 travel budget required by the Omnibus Budget Reconciliation Act of 1981, the amount of travel dollars spent per employee increased by 43 percent between 1980 and 1985, while prices for travel services during the same period increased by only 36 percent. Although the improvements implemented by GSA and DoD have eliminated some travel expenses, the General Accounting Office states that additional changes in travel management could produce further savings.

Proponents argue that an across-the-board reduction in 1987 would prompt agencies to pursue cost-saving practices more aggressively. Possibilities include better monitoring of costs, elimination of low-priority travel, and greater use of innovative procurement methods like negotiated discounts for high-volume travel. With improved management, they say, agencies could achieve reductions without significantly cutting back travel.

On the other hand, enactment of a 10 percent travel limitation runs the risk of creating difficulties for programs that rely heavily on travel for effective management. Agencies with many field offices or contractors, for example,

may face inefficiencies or added costs in other areas if required to make cuts in travel. Opponents of a limitation on travel point out that the risk of inefficiencies increases as possible management improvements and cuts in low-priority travel are exhausted. Additionally, some substitutes for travel, such as telecommunications equipment purchases, could prove more costly. From this perspective, singling out travel is less preferable than a general reduction in administrative expenses, the approach taken in the Balanced Budget and Emergency Deficit Control Act of 1985. Finally, some would argue that limitations in military travel would interfere with national defense activities. If military travel was exempted from the 10 percent reduction, however, the budgetary savings would greatly diminish.

REVENUES

This category presents 35 options for increasing revenues from federal taxes. The first three options concern increases in income tax rates for individuals and corporations. Options numbered REV-04 through REV-06 discuss taxes on consumption, including a new value-added or retail sales tax, new or increased taxes on energy, and extensions or increases of existing excise taxes.

Most of the options suggest ways to broaden the base of the income tax, by reducing or eliminating the revenue losses stemming from tax preferences. REV-07 through REV-09 would reduce investment tax preferences that were created to encourage capital formation generally. REV-10 through REV-15 would alter tax preferences aimed at particular industries or activities. REV-16 through REV-20 would reduce preferences that make some forms of saving more attractive than others. The remaining options for broadening the income tax base (REV-21 through REV-29) concern tax preferences that do not directly encourage saving or investment.

Other options include REV-30, which is aimed at improving compliance with income tax laws; REV-31 and REV-32, which describe ways to reduce most tax preferences through across-the-board percentage cuts or by imposing minimum taxes; REV-33 and REV-34, which describe ways to reduce the revenue loss attributable to the possessions and foreign tax credits; and REV-35, which would reduce the tax preference for passing appreciated capital assets to one's heirs.

The discussions of base-broadening options refer to, and in some cases duplicate, the provisions of the President's tax reform proposal [1/] and the tax reform bill passed by the House in December 1985 (H.R. 3838). The revenue estimates in this volume for each option assume that other provisions of the tax law, including the rate structure, are unchanged. Thus, they may differ from estimated effects of similar provisions in the reform proposals, which may have been estimated under a different rate structure and different effective dates and transition rules.

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1. *The President's Tax Proposals to the Congress for Fairness, Growth, and Simplicity* (May 1985).

The estimates of revenue gains from all of the options were made relative to the CBO baseline budget forecast. The baseline is developed under the assumption that most provisions of the tax code that are currently scheduled to expire, or that expired on December 31, 1985, will not be extended or reinstated. If, for example, tax preferences scheduled to expire between 1986 and 1991 were extended, they would make a difference of $32.0 billion in fiscal years 1987-1991 relative to the CBO baseline. These tax preferences and other provisions scheduled to expire in future years are described in CBO's report, *The Economic and Budget Outlook: Fiscal Years 1987-1991*, pp. 104, 105.

Most of the options have an effective date of January 1, 1987. For a few of the options (primarily those affecting taxes on consumption), an earlier date of October 1, 1986, is assumed in order to increase revenue yields in 1987. A January 1, 1988, effective date is assumed for REV-04 (the value-added tax) because it is believed this option cannot be implemented immediately.

REV-01 RAISE MARGINAL TAX RATES FOR INDIVIDUALS

Addition to CBO Baseline	Annual Added Revenues (billions of dollars) 1987	1988	1989	1990	1991	Cumulative Five-Year Addition
Raise Marginal Tax Rates 5 Percent	13.3	19.1	20.6	22.1	23.8	98.9
Raise Marginal Tax Rates 10 Percent	26.7	38.4	41.3	44.4	47.7	198.5

Under the current income tax structure, marginal tax rates range from 11 percent to 50 percent. (The marginal rate is the rate of tax that a person must pay on an extra dollar of income.) A 10 percent across-the-board increase in marginal tax rates, raising them to between 12 percent and 55 percent, would increase revenues by almost $200 billion between 1987 and 1991.

The main advantage of increasing marginal tax rates is that it could raise a significant amount of money quickly and easily. Raising tax rates is quite straightforward administratively. Because the bulk of the income tax is collected in the form of payments withheld from employee paychecks, the added revenue would begin to flow into the Treasury as soon as employers changed their payroll accounting practices (usually in one to three months). In addition, because the income tax is progressive, even after accounting for exemptions and deductions, higher marginal rates would result in a greater proportionate reduction in after-tax income for upper-income than for low-income people.

A rate increase may have undesirable effects, however. Most taxpayers have marginal rates that are fairly high, compared with historical levels, despite the reductions enacted in 1981. High marginal rates may discourage working, saving, and investing, and raising them would make this problem worse.

Higher tax rates would also exacerbate economic distortions resulting from provisions that discriminate among sources and uses of income. These provisions reduce economic efficiency by biasing the allocation of resources toward tax-favored activities. Increases in tax rates on those in the top brackets can especially distort savings and investment decisions.

In addition to their economic costs, tax rate increases may be perceived as unfair because they most heavily affect people who are already paying taxes, especially those who now pay at high rates. Taxpayers who are able to reduce their tax bill (or escape taxation altogether) by taking advantage of special provisions of the law are significantly less affected (or not affected at all). If the tax base were broadened by eliminating some or all of these special provisions, as is proposed in most current tax reform plans, then subsequent tax rate increases might not be as unfair because most (if not all) taxpayers would share the additional burden.

Raising marginal income tax rates is contrary to the goals of current efforts to reform the income tax system. All major tax reform proposals would broaden the tax base, decrease the number of tax brackets, and reduce the statutory rates. If marginal rates were raised, subsequent attempts to broaden the tax base might be received with less enthusiasm because, at higher rates, each base-broadening change in the system would cost taxpayers comparatively more.

REV-02 AMEND OR REPEAL INDEXING OF INCOME TAX RATES

Addition to CBO Baseline	Annual Added Revenues (billions of dollars) 1987	1988	1989	1990	1991	Cumulative Five-Year Addition
Repeal Indexing	4.4	12.7	23.6	36.7	51.9	129.3
Delay Further Indexing Until January 1, 1988	4.4	7.3	7.8	8.5	9.1	37.1
Index for Inflation in Excess of 3 Percent	3.8	10.4	18.1	27.0	37.4	96.7

This year, as in 1985, the rate structure of the individual income tax will be adjusted to offset the effects of recent inflation. The personal exemption and the boundaries of each statutory tax bracket (including the zero bracket amount) were increased 4.08 percent in 1985 and will be increased 3.7 percent this year to reflect the change in the Consumer Price Index experienced during the previous years. A similar adjustment will be made annually in future years.

Many changes have been proposed to reduce the effects of indexing. Ideas include outright repeal, delay of indexing, and partial indexing for inflation above some threshold rate only. The additional revenues that would result from three frequently discussed proposals are shown in the table above.

Changes in indexing would gain smaller amounts of revenue in their first year of enactment, but would raise considerably larger amounts in future years because of the cumulative effects of indexing. The significant reduction in the deficit, especially in later years, is one of the main arguments in favor of cutting back on indexing.

Another advantage of amending or repealing indexing is that it would not single out any particular group of taxpayers, but rather would apply to everyone by changing the tax structure across the board. In addition, it would be easy to carry out administratively. Repeal or delay of indexing could be accomplished simply by not changing the bracket boundaries and the personal exemption for one or more years. Indexing for inflation in excess of a specified rate would be done precisely as indexing is done now,

except that a smaller percentage change would be applied to the exemption amount and the bracket boundaries.

Arguments against changing indexing are both economic and political. In economic terms, reducing indexing would increase marginal tax rates for many taxpayers by allowing inflation to move them into higher tax brackets even when their incomes in constant dollars were unchanged. Therefore, it would reduce economic efficiency to the extent that higher marginal tax rates bias the allocation of resources toward tax-favored activities, and could also reduce work effort and saving. At the same time, the incentive effects of reducing indexing would not be exactly the same as for explicit across-the-board increases in marginal tax rates. For example, taxpayers in the 50 percent bracket would not experience an increase in their marginal tax rate, even though their average tax rate would rise.

On political grounds, proponents favor indexing because it requires the Congress to decide explicitly on tax increases. Without indexing, inflation causes more-than-proportional increases in tax liabilities as incomes rise. This results in increased real tax burdens without legislative action even though real income increases may not have occurred. In contrast, indexing forces the Congress to enact tax increases if it wants to increase the ratio of federal revenues to GNP; it must then decide directly about the desirability of a larger public sector. Conversely, an unindexed tax system provides a politically easy way to raise revenues and lower deficits.

The revenue gains from either complete elimination of indexing or delay of indexing for one year would be highly sensitive to inflation; for higher rates of inflation, the revenue increase from eliminating indexing would be greater. (This also means that, in the absence of indexing, average tax rates paid by individuals would rise much faster if inflation increased.) On the other hand, the revenue pickup compared with current law from indexing for inflation in excess of 3 percent would be less sensitive to changes in inflation (unless inflation fell below 3 percent), and taxpayers would still be somewhat protected from the effects of increases in the rate of inflation.

Both elimination of indexing and a uniform percentage increase in marginal tax rates would increase taxes more for high-income than for low-income taxpayers, both in absolute terms and as a percentage of income (see REV-01). In that sense, both ways of raising tax rates would reduce inequality in the after-tax distribution of income. For the same revenue gain, however, elimination of indexing would increase taxes relatively more for low-income people than would a constant percentage increase in marginal tax rates. This would occur mainly because a smaller proportion of

low-income families itemize than do high-income families. If indexing were eliminated, nonitemizers would lose the benefit of increases in both the personal exemptions and the zero bracket amount (ZBA), while itemizers would not be affected by the failure to index the ZBA. As a result, the percentage increase in taxes paid would be greater for nonitemizers (mostly low- and middle-income) than for itemizers (mostly high-income).

REV-03 IMPOSE A CORPORATE SURTAX

Addition to CBO Baseline	Annual Added Revenues (billions of dollars) 1987	1988	1989	1990	1991	Cumulative Five-Year Addition
Surtax on Tax Before Credits						
10 Percent	7.8	13.9	15.1	15.8	16.1	68.8
5 Percent	3.9	6.9	7.5	7.8	7.9	33.9
Surtax on After-Tax Economic Income						
5 Percent	10.8	18.3	20.7	23.3	24.9	97.9
2.5 Percent	5.4	8.8	10.0	11.3	12.1	47.6

Imposing a corporate surtax has recent historical precedent. As a temporary measure to help pay for the Vietnam War, a surtax was imposed on individual and corporate taxes from January 1, 1968, to December 31, 1969, at the annual rate of 10 percent, and from January 1, 1970, to June 30, 1970, at the annual rate of 5 percent. For most corporate taxpayers, a 10 percent surtax comparable to the Vietnam War surtax would be equivalent to raising the marginal statutory tax rate 4.6 points--from 46 percent to 50.6 percent. A 10 percent surtax would raise almost $70 billion between 1987 and 1991; a 5 percent surtax would raise $34 billion over the same period.

A surtax is a relatively simple means of raising a significant amount of revenue quickly, and in a way that may be temporary if desired. Proponents of a surtax on individual incomes generally include a corporate surtax at the same rate on grounds of equity. The principal objection to a surtax is that it increases the tax burden most for those firms that already pay the most taxes, thereby exacerbating a major problem of the current corporate income tax--that it results in widely differing effective tax rates, both across and within industries. Moreover, if the surtax was temporary, provisions in current law that allow deferrals of taxable income, such as accelerated depreciation, could become forgiveness rather than deferral of surtax liability. This would further increase the value of these tax preferences and the unevenness of the corporate tax burden.

An alternative is to impose a surtax on a comprehensive measure of after-tax income. For example, the surtax could be imposed on business

receipts minus allowable business expenses such as wages and salaries, cost of materials, payments to qualified pension plans, and straight-line depreciation of business assets. Asset lives would be approximated by 40 years for structures and by midpoint lives for equipment under the Asset Depreciation Range (ADR) system in effect before 1981. Thus, for this surtax, the tax base would become income already subject to the regular tax plus fringe benefits and most business tax preferences; it could be reduced by the regular income tax, and by an exclusion of $100,000. Imposition of a 5 percent surtax on this base would raise $98 billion between 1987 and 1991; if the rate was 2.5 percent, the net revenue increase would be $48 billion.

The advantage of this approach is that such a surtax, which can also be described as an additional minimum tax on after-tax economic income, would fall most heavily on those corporations that currently make considerable use of tax preferences. Thus, unlike the surtax on tax before credits, it would reduce the value of those corporate preferences. It would tax all income above the exclusion, including income sheltered from the regular tax by deferrals. If a corporation had an effective tax rate of 46 percent on its economic profits, a 5 percent surtax on economic income would increase its effective rate 2.7 points, to 48.7 percent. If it had an effective tax rate of zero, this surtax would increase its effective rate to 5 percent.

One objection to a surtax on after-tax economic income is that it would raise corporate taxes even for those corporations not using tax preferences, although by a lesser amount than a surtax on tax liability that raised the same net revenue. Alternatives that would raise taxes only for those corporations using preferences to reduce tax liability are discussed in REV-31 and REV-32.

REV-04 IMPOSE A VALUE-ADDED OR NATIONAL SALES TAX

Addition to CBO Baseline a/	Annual Added Revenues (billions of dollars) 1987	1988	1989	1990	1991	Cumulative Five-Year Addition
5 Percent Tax, Comprehensive Base	--	71.2	107.7	115.8	124.8	419.5
5 Percent Tax, Narrower Base, Exemptions for Food, Housing, and Medical Care	--	42.4	64.1	69.0	74.3	249.8
5 Percent Tax, Narrower Base, No Exemptions for Food, Drugs, and Medical Care; Low-Income Relief Under Means-Tested Programs b/	--	56.0	84.9	91.2	98.1	330.2

a. Estimates based on effective date of January 1, 1988.

b. Includes increased outlays for Medicaid, Food Stamps, Medicare, Supplemental Security Income, and Aid to Families with Dependent Children.

A national value-added or retail sales tax could raise substantial revenue at relatively low tax rates. A common way of administering a value-added tax is to collect a tax on the total value of sales of all firms, but allow them to claim a credit for taxes paid on goods purchased from other firms. Creditable purchases include those of natural resources (including energy), intermediate materials, and capital goods. Wages, salaries, profits, and interest are not creditable because they have not been previously taxed and represent the "value added" by a firm.

A value-added tax (VAT) is essentially equivalent in economic effect to a national retail sales tax. Either type of tax could be fully comprehensive, or could allow exemptions for certain goods and services. In addition to exemptions for charitable, religious, and educational institutions, the tax might allow exemptions for necessities, thereby reducing the regressivity of

the tax. These might include food consumed at home, all housing, and medical services, among others. Ease of administration might also justify exemptions for items such as the imputed value of services of financial institutions, the imputed rent from owner-occupied housing (though sales of new homes could be taxed), and sales by small businesses and farms.

Currently, the United States relies much less on consumption taxes than do most other countries belonging to the Organization for Economic Cooperation and Development (OECD)--many of which already impose a VAT. A major argument for introducing a VAT or national retail sales tax to raise a significant amount of revenue in this country is that it would be more neutral among economic activities than an equal-revenue increase in income tax rates. In addition, a VAT or retail sales tax would be neutral between present and future consumption, and therefore would not adversely affect incentives for saving and investment as much as an equal increase in income taxes. (Like an income tax, however, it would reduce rewards from work effort.) Some people also favor a VAT or a sales tax because it taxes imports and exempts exports, which could improve the nation's trade balance. Finally, there is some evidence from public opinion polls that the public regards increases in sales taxes as a fairer way of raising revenue than increases in the income tax.

The major argument against a national sales tax is that it is regressive because it must be imposed at a flat rate and because the ratio of consumption to income falls for people in higher income classes. The regressivity of a sales tax may be overstated, however, by using current rather than lifetime income as a measure of ability to pay and, in any case, is mostly correctable as explained below. Other arguments against a national sales tax are that any increase in the price level it induces might have further inflationary repercussions, and that states would regard a federal sales tax as interfering with their traditional revenue base. In addition, a federal sales tax would require new enforcement procedures and additional IRS personnel and might take one or two years to implement fully; therefore, it should be considered only as part of an effort to raise a significant amount of revenue. (For example, the Department of Treasury has estimated that a VAT would require 20,000 additional personnel at a cost of $700 million.) Finally, the revenue-raising potential of a federal sales tax is a concern among those who fear it might facilitate undue growth of the federal government.

The regressivity of a value-added tax could be alleviated by exemptions for goods and services consumed by low-income persons. Such exemptions would, however, substantially increase costs of enforcement and compliance, especially over time as new items considered worthy of special

treatment were added to the list. An alternative approach to offsetting regressiveness that would be easier to administer is to allow additional exemptions or credits for low-income people under the federal income tax.

The derivation of two tax bases for a VAT is shown in the accompanying table. The first base is as broad as possible, excluding only those items that would be administratively very difficult to include. The second adds exemptions for food, health care, and other expenditures. For 1984, the comprehensive base is equal to $2.1 trillion, while the more narrowly defined base amounts to $1.3 trillion.

A 5 percent tax on the comprehensive VAT base would raise an estimated $71 billion in fiscal year 1988 and $420 billion over the 1987 to 1991 period, net of reduced personal and corporate income taxes. (Personal and corporate taxes would be reduced by a VAT because the tax would reduce personal and corporate incomes, assuming nominal GNP remained constant.) The narrower-based VAT would raise $42 billion in fiscal year 1988 and $250 billion between 1987 and 1991. This estimate assumes that collections would not begin until January 1, 1988.

A third option is to include food and medical care in the narrower tax base, but to provide low-income relief through payments to low-income individuals through means-tested programs such as Medicaid, Aid to Families with Dependent Children (AFDC), Supplemental Security Income (SSI), and Food Stamps. Since medical care would be subject to the VAT, Medicaid and Medicare benefits would automatically be adjusted to reflect the tax. A 5 percent increase in Food Stamp, AFDC, and SSI benefits would compensate low-income persons for taxes on food, as well as partially offset taxes on other purchases. After accounting for the costs of these additional outlays, this option would reduce the deficit by $56 billion in 1988, and about $330 billion in the years 1987 through 1991.

Value-added taxes have been the subject of recently proposed legislation in other contexts. In 1985, the Senate passed a bill that included a low-rate (0.08 percent) VAT on manufacturers to finance additional Superfund outlays. The tax would be limited to manufacturing companies with sales of over $5 million. Another, more comprehensive, VAT--referred to as a business transfer tax (BTT)--has been proposed in the Senate (S. 1102). The BTT in its most recent version is a broad-based VAT with a tax rate between 7 percent and 10 percent. The BTT's receipts would be used to finance lower individual and corporate tax rates, more generous capital recovery provisions, and expanded IRA accounts for individual savers. Depending on the tax rate, any net revenue from the BTT could be used for deficit reduction.

CALCULATION OF TAX BASE UNDER A VAT, 1984

Items Included		Amount (In millions of dollars)	Gross Tax at 5 Percent Rate (In millions of dollars)
Total Personal Consumption in GNP		2,341,781	
Less:	Rent on housing	397,873	
	Net foreign travel expenditures	11,240	
	Religious and welfare activities	35,165	
Plus:	Monetary interest paid by individuals	77,800	
	New residential construction	149,874	
Comprehensive VAT Tax Base		2,125,177	106,259
Possible Exemptions			
	New residential construction	149,874	
	All medical care	258,309	
	Food purchased for off-premise consumption	311,035	
	Food furnished employees	6,797	
	Clothing issued to military personnel	120	
	Domestic services	8,075	
	Financial services provided free of charge	55,822	
	Expense of handling life insurance	26,621	
	Local transit (excluding taxis)	4,069	
	Clubs and fraternal organizations	3,139	
	Private education and research	35,403	
Narrower VAT Tax Base		1,265,913	63,296

SOURCE: Congressional Budget Office.

REV-05 INCREASE ENERGY TAXES

Addition to CBO Baseline	Annual Added Revenues (billions of dollars) 1987	1988	1989	1990	1991	Cumulative Five-Year Addition
Impose Tax on Domestic and Imported Oil ($5 per barrel)	20.4	21.8	22.1	22.5	22.9	109.7
Impose Oil Import Fee ($5 per barrel)	7.4	7.3	7.4	7.8	7.9	37.8
Impose Excise Tax on Natural Gas ($1 per 1,000 cubic feet)	12.0	12.9	13.2	13.6	13.7	65.4
Increase Motor Fuel Excise Tax (12 cents per gallon)	10.4	10.7	10.9	10.9	10.9	53.8
Impose Broad-Based Tax on Domestic Energy Consumption (5 percent of value)	13.9	15.2	16.2	17.3	18.5	81.1

NOTE: These added revenues are net of any estimated changes in income, windfall profit, and other taxes that might result from each option. Induced outlay effects are not estimated. These estimates are based on CBO's baseline oil price forecast of $23.60 per barrel in 1987, rising to $27.50 per barrel by 1991. To the extent that oil prices differ from this forecast, revenues may be significantly affected. The effective date for all of these proposals is October 1, 1986.

Energy taxes could raise significant amounts of revenue, reduce the country's dependence on foreign oil suppliers, and increase conservation by making energy more expensive. The United States depends on foreign sources for about 30 percent of the oil it consumes, and about 11 percent of its total energy. This dependence exposes the U.S. economy to potential supply interruptions.

Reducing energy consumption by raising energy taxes might reduce the costs of supply interruptions and increase the flexibility of U.S. foreign policy. Moreover, reduced demand for imported oil resulting from an energy tax could force foreign suppliers to absorb part of the tax through lower prices. Finally, energy taxes (by raising energy prices) would help preserve the conservation gains that have been achieved in recent years and that might otherwise be lost as a consequence of lower oil prices.

Concern has been expressed over the use of energy taxes, on several grounds. Because they would raise energy prices, these taxes would more heavily burden low-income taxpayers who spend a relatively high percentage of their income on energy. Moreover, energy taxes could have widely different effects on firms and households in different parts of the country. In addition, to the extent that the imposition of energy taxes might raise the Consumer Price Index, indexed federal outlay programs would be affected. Finally, some observers have argued that stockpiling oil is a more cost-effective way of relieving dependence on imports that would not artificially reduce current energy use by households and businesses, and that, for the rest, free markets provide sufficient incentives for resource conservation.

Five different energy taxes are considered below.

Impose Excise Tax on Domestic and Imported Oil. An excise tax on all oil--both domestically produced and imported--could raise substantial revenue. A $5-per-barrel tax would raise about $22 billion per year and would equal more than 25 percent of the current spot price of a barrel of oil or 12 cents per gallon of gasoline.

In 1981, the average cost of a barrel of oil was $35. The current spot price is under $20 and could fall considerably more in the near future. A comprehensive tax on oil of $5 per barrel would partially offset any lowering of prices to consumers, thereby preserving conservation efforts and discouraging consumption, but would still leave prices below 1981 levels. Prices (net of tax) received by domestic oil producers would decline, which could reduce domestic oil production. To the extent that a reduction in U.S. oil consumption occurred, it could result in foreign producers implicitly bearing part of the tax through lower world oil prices. In contrast, prices received by producers of alternative sources of energy (natural gas, coal) would rise, encouraging additional production from those sources.

Impose Oil Import Fee. As an alternative to a broad excise tax on all oil, the Congress could limit the tax to imports of crude petroleum and petro-